

Message Text

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FM AMEMBASSY BELGRADE
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TAGS: ECON, EGEN, YO
SUBJECT: YUGOSLAV ECONOMIC TRENDS THROUGH OCTOBER 1976

REF: BELGRADE A1256

1. SUMMARY. THE YUGOSLAV ECONOMY CONTINUES THE TURNAROUND DESCRIBED IN REFAIR. THE ANNUALIZED COST OF LIVING INCREASE IS 10 PERCENT, THE CURRENT ACCOUNT FOR 1976 SHOULD BE APPROXIMATELY IN BALANCE (WITH THE POSSIBILITY OF A SURPLUS), THE TRADE DEFICIT IS MORE THAN \$1 BILLION LESS THAN ONE YEAR AGO, AND RESERVES ARE AT AN ALL-TIME HIGH OF \$2.8 BILLION. ON THE NEGATIVE SIDE, INDUSTRIAL PRODUCTION IS INCREASING AT HALF THE PLANNED RATE. PRODUCTIVITY IS FALLING, AND PRESSURES FOR PRICE INCREASES CONTINUE TO GROW. END SUMMARY.

2. CURRENT ACCOUNT. DUE PRIMARILY TO A \$1 BILLION REDUCTION IN ITS TRADE DEFICIT IN THE FIRST 10 MONTHS OF 1976 IN COMPARISON WITH THE SAME PERIOD LAST YEAR, BUT ALSO TO INCREASED
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INVISIBLE EARNINGS, YUGOSLAVIA SHOULD END 1976 WITH ITS CURRENT ACCOUNT MORE OR LESS IN ABALANCE. THROUGH OCTOBER, YUGOSLAVIA HAS A CURRENT ACCOUNT SURPLUS OF \$244 MISSION. WHILE THIS FIGURE WILL BE REDUCED IN ANY CASE WITH THE END OF THE SEASONAL INFLUX OF HARD CURRENCY TOURISM EARNINGS, THE REAL DETERMINANT IS THE DEGREE TO WHICH IMPORT

RESTRICTIONS ARE EASED FROM NOW TO YEAR-END. YUGOSLAV OFFICIALS ARE PREDICTING A SURPLUS OF \$50 TO \$100 MILLION, BUT ANY FIGURE BETWEEN THAT AND A DIFICIT OF THE SAME SIZE IS EQUALLY LIKELY.

3. TRADE. THE 1976 TRADE DEFICIT THROUGH OCTOBER WAS \$1.95 BILLION AS COMPARED TO \$3.07 BILLION IN THE SAME PERIOD LAST YEAR. THIS WAS ACCOMPLISHED BY RESTRICTING HARD CURRENCY IMPORTS FROM THE WESTERN DEVELOPED COUNTRIES (DOWN 16 PERCENT), WHILE INCREASING EXPORTS TO THOSE COUNTRIES BY 41 PERCENT. TRADE WITH THE SOCIALIST COUNTRIES INCREASED BY 12 PERCENT, DUE ALMOST ENTIRELY TO INCREASED TRADE IN BOTH DIRECTIONS WITH THE SOVIET UNION. IMPORTS FROM DEVELOPING COUNTRIES DECREASED 4 PERCENT AND EXPORTS TO THESE COUNTRIES INCREASED BY THE SAME MARGIN. TRADE RESULTS IN OCTOBER, HOWEVER, SHOWED A LOWER RATE OF EXPORT GROWTH THAN HAD PREVIOUSLY BEEN THE CASE AND A 9 PERCENT INCREASE IN IMPORTS OVER OCTOBER 1975. AND

ACCENTUATION OF THE IMPORT TREND IS LIKELY IN NOVEMBER AND DECEMBER.

4. INVISIBLES. WORKERS' REMITTANCES THROUGH SEPTEMBER 1976 TOTALLED \$1,455 BILLION, AND INCREASE OF 11.5 PERCENT OVER THE SAME PERIOD LAST YEAR. THIS SHOWS THE CONTINUED SUCCESS OF YUGOSLAV BANKS IN ATTRACTING HIGHER AMOUNTS OF THE SAVINGS OF THESE WORKERS, AS THE ABSOLUTE NUMBER EMPLOYED ABROAD HAS CONTINUED TO DECREASE IN 1976 AT ROUGHLY THE 60,000-80,000 RATE OF THE PAST TWO YEARS. HARD CURRENCY EARNINGS FROM TOURISM DURING THE FIRST THREE QUARTERS INCREASED BY 5.3 PERCENT TO \$617 MILLION (DUE TO PRICE INCREASES), EVEN LIMITED OFFICIAL USE

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THOUGH 7 PERCENT FEWER FOREIGN TOURISTS VISITED YUGOSLAVIA DURING THIS TIME.

5. RESERVES. AS OF THE END OF OCTOBER, YUGOSLAVIA HAD OFFICIAL FOREIGN CURRENCY RESOURCES OF \$2.2 BILLION AND UN-OFFICIAL RESERVES IN THE COMMERCIAL BANKING SYSTEM OF \$600 MILLION. THIS IS ALMOST TWICE AS HIGH AS LAST YEAR AND SIGNIFICANTLY ABOVE THEIR PROFESSED POLICY LEVEL OF ENOUGH RESERVES TO COVER TWO MONTHS OF IMPORTS (ABOUT \$1.2 BILLION). AS A RESULT, NATIONAL BANK AND ASSOCIATION OF BANKS OFFICIALS HAVE INFORMED THE EMBASSY THAT A SELECTIVE BORROWING POLICY HAS BEEN INITIATED WHEREAS ANY FOREIGN CREDITS WOULD BE RELATIVELY LONG-TERM AND AT FAVORABLE INTEREST RATES.

6. INDUSTRIAL PRODUCTION. LACKLUSTER OCTOBER RESULTS (A 2.5 PERCENT INCREASE OVER OCTOBER 1975) HAVE DEFLATED YUGOSLAV HOPES TO ACHIEVE A RATE OF GROWTH OF INDUSTRIAL PRODUCTION IN 1976 MUCH ABOVE 3 PERCENT. STOCKS, WHILE FALLING

FROM THE RECORD HIGH LEVELS OF SUMMER 1976, ARE STILL FAR TOO HIGH. STRICTER REGULATION OF INVESTMENT AND UNCERTAINTIES REGARDING THE FIVE-YEAR PLAN CONTINUE TO HAMPER CAPITAL INVESTMENT AND THUS INDUSTRIAL PRODUCTION AS WELL.

7. PRICES. THE COST OF LIVING INCREASED 3.7 PERCENT IN NOVEMBER DUE LARGELY TO LARGE INCREASES IN THE PRICE OF BREAD AND FLOUR. THESE STAPLES ARE HEAVILY WEIGHTED IN ALL PRICE INDICES, CAUSING RETAIL PRICES TO JUMP 2.3 PERCENT AND PRODUCER PRICES BY 1.4 PERCENT. DESPITE THIS JUMP RETAIL PRICES AND PRODUCER PRICES WERE ONLY 8.4 PERCENT AND 7 PERCENT HIGHER THAN A YEAR EARLIER, RESPECTIVELY. THE COST OF LIVING OVER THIS PERIOD ROSE 10.1 PERCENT. THE GOVERNMENT GOAL OF AN INFLATION RATE OF 10 PERCENT FOR THE YEAR IS LIKELY TO BE ACHIEVED, AS NO NEW MAJOR PRICE INCREASES HAVE BEEN ANNOUNCED FOR 1976.

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THE ANNOUNCED GOVERNMENT INTENT TO KEEP 1977 PRICE INCREASES AT THE 1976 RATE FACES MUCH TOUGHER GOING. ADMINISTRATIVE MEASURES HAVE BEEN PRIMARILY RESPONSIBLE FOR THE SUCCESS OF THE PRICE STABILIZATION PROGRAM AND INFLATIONARY PRESSURE IS STRENGTHENING. NUMEROUS PRICE INCREASE REQUESTS, REPORTS OF BUSINESS LOSSES, INCREASING EMPLOYEE SALARIES, THE POTENTIAL INCREASE IN OIL IMPORT PRICES, GROWING INEQUITIES OF THE PRICE CONTROLS SYSTEM, AND THE INCREASE OF OVER 50 PERCENT IN MONEY SUPPLY (CURRENCY PLUS DEMAND DEPOSITS) OVER THE PAST YEAR MAKE NEXT YEARS CONTROL OF PROCES MUCH MORE

DIFFICULT THAN HAS BEEN THE CASE TYNIS FAR.

8. INVESTMENT. DESPITE STATISTICS THAT SHOW A HIGH RATE OF GROWTH OF INVESTMENTS (36 PERCENT INCREASE IN FIRST NINE MONTHS OF 1976), YUGOSLAV OFFICIALS CONTEND THAT ONLY PAYMENTS FOR PAST INVESTMENTS GREW AND NOT REAL INVESTMENT. THIS IS ATTRIBUTED TO THE STRICT PAYMENT REQUIREMENTS OF THE NEW ACCOUNTING AND PAYMENTS LAW AND IS CITED AS THE MAJOR REASON FOR THE LACK OF GROWTH OF INDUSTRIAL PRODUCTION. UNCERTAINTIES REGARDING INVESTMENT UNDER THE 1976-80 FIVE-YEAR PLAN ARE LIMITED OFFICIAL USE
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CONTINUING TO PUT A DAMPER ON NEW INVESTMENT. INSTEAD OF THE 8 PERCENT INCREASE IN REAL INVESTMENTS IN THE ECONOMY PLANNED FOR 1976, YUGOSLAVS ARE NOW STATING THAT ONLY A TWO TO THREE PERCENT INCREASE IS EXPECTED. THE FEDERAL CHAMBER OF ECONOMY REPORTED THAT THE VALUE OF REGISTERED INVESTMENT PROJECTS OVER THE FIRST 10 MONTHS OF 1976 WAS ONLY 65 PERCENT OF THE SUM REGISTERED IN THE FIRST SEVEN MONTHS OF 1975.

9. COMMENT: YUGOSLAV EXTERNAL ACCOUNT AND INFLATION STATISTICS FOR 1976 ARE MOST NOTABLE BECAUSE THEY SHOW THAT THE GOVERNMENT HAS THE WILL AND THE ABILITY TO QUICKLY RECTIFY WHAT IT CONSIDERS TO BE DANGEROUS TRENDS IN THE ECONOMY. THEIR SUCCESS, HOWEVER, WAS MAINLY DUE TO ADMINISTRATIVE MEASURES. THE STRUCTURAL WEAKNESSES IN THE ECONOMY, SUCH AS OVERCAPACITY OR UNDERCAPACITY IN SEVERAL INDUSTRIAL SECTORS AND INEFFECTIVE UTILIZATION OF FACTORIAL BASE, REMAIN STRONG AND ESSENTIALLY UNCHANGED. (TWO TIGHTENING MEASURES WHICH HAVE BEEN MADE ARE THE NEW ACCOUNTING AND PAYMENTS LAW, AND THE REQUIREMENT THAT CAPITAL INVESTMENTS MUST BE REGISTERED WITH THE FEDERAL CHAMBER OF ECONOMY). THE ECONOMY IS NOW REACHING THE POINT WHERE MORE DIRECTION IS NEEDED TO GUIDE THE STABILIZATION PROGRAM TOWARDS THE TARGETS SPECIFIED IN THE FIVE-YEAR PLAN. UNFORTUNATELY, THE POLICY SEEMS LIMITED TO "MORE OF THE SAME". THE DRAFT RESOLUTION FOR 1977 CALLS FOR PRICE INCREASES LIMITED TO THIS YEAR'S RATE AND A LIMITED GROWTH OF IMPORTS, BUT DOES NOT FOCUS ON POTENTIAL PROBLEMS WITH INDUSTRIAL PRODUCTION WHICH MAY RESULT. THE FAILURE TO DATE TO COMPLETE THE SOCIAL ACCORDS WHICH WERE INTENDED TO PROVIDE DETAILED INVESTMENT GUIDELINES IN PRIORITY SECTORS UNDER THE FIVE-YEAR PLAN LEAVES INVESTMENT IN A HOLDING PATTERN. THE PROLIFERATION OF NEW LAWS ALREADY PASSED AND TO BE PASSED WILL CREATE SOME INITIAL CONFUSION IN THE ECONOMY. THE PRICE CONTROL PROGRAM WILL BE INCREASINGLY DIFFICULT TO MANAGE. UNTIL THESE PROBLEMS ARE SORTED OUT, IT IS DIFFICULT TO SEE HOW THE ECONOMY COULD MOVE FORWARD AT THE DYNAMIC RATE TO WHICH THE YUGOSLAVS HAVE LIMITED OFFICIAL USE
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